



Investment Office

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December 15, 2008

AGENDA ITEM 3e

TO: MEMBERS OF THE INVESTMENT COMMITTEE

- I. SUBJECT:** Consultant Conflict of Interest Protocol Update
- II. PROGRAM:** Policy and Business Support
- III. RECOMMENDATION:** Information
- IV. ANALYSIS:**

The CalPERS Consultant Conflict of Interest Protocol (Protocol), adopted by the Committee in 2005, requires CalPERS Investment Consultants to disclose on an ongoing basis any circumstance that may create actual, potential, or perceived conflicts of interest. The Protocol requires Staff to report annually, or as needed, to the Investment Committee a summary of the types of disclosable interests reported by the consultants in the prior year and the actions taken by Staff in response to the disclosable interests. A copy of the Protocol is provided as Attachment 1.

In compliance with the Protocol, Staff monitors each consultant's compliance through its internal conflict of interest tracking process. At least once a year, Staff reviews and discusses with each consultant all disclosable interests and the cumulative effect of each disclosure.

For the period from July 1, 2007 through November 30, 2008, three firms in the Alternative Investment Management (AIM) Consultant Pool and the Primary Pension Consultant filed disclosures under the Protocol. Staff consulted with CalPERS Legal Office on the disclosures summarized below:

- An AIM consultant disclosed that its parent company has an affiliate entity which acts as a placement agent for private equity funds. On occasion, the placement agent has introduced funds to CalPERS. Full disclosure of

the ownership relationship was made to CalPERS at the time of applying and entering into the AIM Consultant Pool. Staff continues to monitor the situation to ensure the relationship does not create conflicts of interest.

- Another AIM consultant was hired to perform valuation services for a direct investment transaction. The consultant is a leading provider of valuation services, has opined on previous AIM transactions and is the best qualified firm in the AIM Pool to perform this work. The consultant disclosed that it had performed financial advisory services for affiliates of the company under consideration for a direct investment. Staff discussed this potential conflict with the CalPERS Legal Office, its advisors and consultants, and disclosed the issue to the Investment Committee in December 2007. Staff determined that the consultant could provide an experienced and fair opinion that would provide additional integrity to the transaction.
- Another AIM consultant disclosed that it is partly owned by a private equity partner in the AIM portfolio. The consultant provides monitoring services for this private equity partner as well as CalPERS. Because of this relationship, Staff has excluded the consultant from the investment decision process with the private equity partner, and has utilized a different consultant to perform due diligence on the partner and its affiliates. In addition, the consultant disclosed it provides fund administration, investment reporting and monitoring to an additional private equity partner in the AIM portfolio. Staff has excluded the consultant from performing monitoring services for the partner.
- In connection with the development by the Supplemental Income Plans (SIP) Division of new target date funds, the Primary Pension Consultant disclosed that its firm offered products and services related to target date funds. After consultation with the Legal Office, staff determined to use an alternative consultant to assist the SIP and Investment Office in developing its new funds.

Additionally, the Investment Committee's Primary Pension Consultant provides the Investment Committee disclosure of its relationships with external managers on an ongoing basis. The disclosures are reported to the Investment Committee in agenda items as the events occur.

V. STRATEGIC PLAN:

Goal II. Foster a work environment that values quality, respect, diversity, integrity, openness, communication, and accountability.

Goal VIII. Manage the risk and volatility of assets and liabilities to ensure sufficient funds are available, first, to pay benefits and second, to minimize and stabilize contributions.

VI. RESULTS/COSTS:

There are no costs associated with this agenda item.

Matt Flynn, Division Chief
Operations, Performance & Technology

Anne Stausboll
Interim Chief Investment Officer